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Report Highlights:
Post forecasts Chinese milk production will reach 30.5 million metric tons in 2011, up five percent from 2010, as local producers gradually rebuild China's dairy herd from the sharp reductions after the 2008 melamine crisis. Whole milk powder production is expected to top one million tons in 2011, up five percent from the year before. China's imports of whole milk powder will likely exceed 400,000 tons in 2011, more than double the level in 2009, due to rising sales of a wide variety of dairy foods. Nonfat milk powder imports will also continue to grow, fueled by particularly strong demand from infant formula manufacturers.

Executive Summary

Post forecasts Chinese milk production will continue modest growth in 2011, up five percent to 30.5 million metric tons. Local producers are slowly rebuilding the Chinese dairy herd following the melamine crisis, when 15 percent of China's dairy cows were taken out of production due to weak demand. While Chinese milk production is on the rise, growth is being hindered this year by additional detections of melamine in Chinese milk powder, animal disease, and comparatively low animal productivity. Output will remain below pre-melamaine levels of more than 35 million tons in 2008 for the foreseeable future.

China's whole milk powder production will increase five percent to over one million tons in 2011, following a two percent rise in 2010. Nonfat dry milk production will be roughly unchanged at 56,000 tons following flat growth in 2010. Imports of milk powder will continue strong gains and account for most of the growth in Chinese milk powder consumption. In 2011, imports of whole milk powder are forecast to top 400,000 metric tons, while imports of nonfat milk powder will reach 100,000 metric tons. Both are more than double sales in 2009. The gains are being driven by overall strong dairy product demand and a superior safety image over local powder. .

Post forecasts China's fluid milk imports in 2011 will grow 13 percent to 17,000 MT, with rising demand among wealthy Chinese and expats. China's fluid milk exports are estimated to reach 14,000 metric tons in 2011, with Hong Kong accounting for almost all sales. China's whole milk powder exports will remain weak at 3,000 MT, a 90 percent decline from pre-melamine export levels.

Production

Cow Milk Production Up in 2011, but Still Far Below Pre-Melamine Levels

Post forecasts Chinese milk production will continue modest growth in 2011, up five percent to 30.5 million metric tons. Despite the increase, output will remain below production of more than 35 million tons before the melamine crisis in 2008. Local producers are slowly rebuilding the Chinese dairy herd following the crisis, when 15 percent of China's dairy cows were taken out of production due to weak demand. Encouraged by higher milk prices in China (up one-third from September 2009 to 3,000 yuan ($441) per metric ton), operators are rapidly increasing imports of dairy cows, which are expected to approach 90,000 head in 2010, more than double the level the year before.

While higher prices and strong long-term prospects for Chinese dairy demand are driving production gains, output growth continues to be dampened by consumer safety concerns for local milk as a result of additional detections of melamine in the past year. Significant findings by Chinese food safety authorities include: August 2010 – 26 metric tons of contaminated product, Shaanxi; July 2010 – 76 metric tons, Qinghai; February 2010 – 165 metric tons, Ningxia; December 2009 – quantity unknown, Shanghai.

Continued detections have lowered processor confidence, with some manufacturers shifting entire product lines to imported ingredients. Fueled by strong demand for alternatives to local supplies, imported milk powder has accounted for nearly all the growth in Chinese milk powder consumption since 2008. Continued illegal use of contaminated milk powder produced before the 2008 crisis in 2011

may hinder industry efforts to improve the safety profile of Chinese milk and dampen output gains for the foreseeable future.

State Council Orders Stricter Melamine Controls

On September 25, the State Council issued "Notification to Further Strengthen Safety and Quality of Dairy Product Production", aimed to prevent further distribution of contaminated milk. The order will require manufacturers to strengthen melamine controls by keeping complete records of inputs and to test for melamine in all dairy products prior to distribution. The new order takes effect at the end of October. Processors have expressed concerns the new measure will hurt sales by raising costs and consumer prices, which are already up substantially from the year before.

FMD Threatens Milk Output Growth

Meanwhile, in addition to consumer safety concerns, producers are also being challenged by higher incidences of animal disease, which may hamper production growth into 2011. By the end of August 2010, nine provinces had officially reported foot and mouth disease (FMD) outbreaks. While it is difficult to estimate the number of animals infected or culled, Post has received unconfirmed reports of mass slaughter in several provinces, and in some cases involving use of the Chinese military to ensure herd elimination. During February-May 2010, the Ministry of Agriculture imposed a rarely used nationwide suspension of transporting dairy and breeding cows due to FMD concerns.

Whole-Fat Milk Powder Production to Rise Five Percent in 2011 while Non-Fat Powder Output to be Unchanged

Post forecasts whole-fat milk powder production will increase five percent to over 1 million tons, following a two percent rise in 2010. Production gains for nonfat dry milk will be roughly unchanged at 56,000 tons following flat growth in 2010. Strong prices for a range of food products that use whole milk powder will encourage WMP production gains through 2011. Key channels include yogurt, ice cream and other dairy products, bakeries, chocolates, and functional formulas for specific consumers like school students, pregnant women, aged, sick people. Overall, milk powder demand will be particularly strong from large-sized processing companies, such as Inner Mongolia based Mengniu and Yili, which offer consumers a superior safety profile over smaller companies. Meanwhile, nonfat milk powder production gains will be limited due to weak demand in infant formula channels, where the impact of food safety concerns is greatest, as formula manufacturers are increasingly relying on imported nonfat milk powder. Demand for local nonfat milk powder is also negatively affected by China's growing imports of infant preparations. Sales of finished infant formula and other infant preparations should approach 70,000 metric tons in 2010, almost double the level in 2008.

Government Dairy Plan Sets 2013 Milk Production Target of 48 Million Tons

On June 8, 2010, MOA, the China National Reform and Development Commission, the Ministry of Industrialization and Information, and the Ministry of

Commerce jointly issued the "China National Dairy Development Plan (2009-2013)". A basic target is that by 2013 China's national dairy production will reach 48 million metric tons, nearly double current estimated output. This will be accomplished by raising cow inventory to 15 million head, increasing yield per animal to 5.7 tons, and increase dairy farms with animal size at and above 100 head from 25 percent to 35 percent of China's total dairy operations.

Related to this plan, China has identified national dairy cow advantageous production areas, which cover 313 counties in cities and provinces including Beijing, Tianjin, Shanghai, Shanxi, Hebei, Shandong, Henan, Inner Mongolia, Liaoning, Heilongjiang, Shaanxi, Ningxia, and Xinjiang.

China has also created five dairy production regions for specialization based on local conditions:

- *Northeast - Inner Mongolia Region* (Heilongjiang, Jilin, Liaoning, and Inner Mongolia) will develop larger household farms and mainly produce milk powder, cheese, butter, UHT milk, and reasonable pasteurized milk or yogurt if necessary.

- *North China Region* (Hebei, Henan, Shangdong, and Shanxi) will mainly produce milk powder, cheese, UHT and pasteurized milk, and yogurt with development of sized farms.

- *West Region* (Shaanxi, Gansu, Qinghai, Ningxia, Xinjiang, and Tibet) will develop local-bred dairy cows, and at the same time develop local specialties, such as goat, yak, horse, camel and donkey milk. It will also focus on forage production. Their main dairy products will include milk powder, cheese, butter, and protein powder.

- *South Region* (Hubei, Hunan, Jiangsu, Zhejiang, Fujian, Anhui, Jiangxi, Guangdong, Guangxi, Hainan, Yunnan, Guizhou, and Sichuan) will develop pasteurized milk, cheese and yogurt, and some production of condensed milk, UHT, and milk powder.

- *Large City Surrounding Region* (Beijing, Shanghai, Tianjin, and Chongqing) will mainly focus on pasteurized milk and yogurt production,

Dairy Cow Production Subsidy to Continue in 2011

The primary publicly notified subsidy to encourage higher production is China's dairy cow genetic improvement support fund. Post expects the amount for the program will be at least the funding level in 2010 of RMB260 million ($38.8 million) to encourage higher milk supplies. China's dairy cow production subsidy started in 2005 with RMB15 million ($223,881) covering 675,000 head of Holstein cows in 15 counties in four major dairy producing provinces including Heilongjiang, Inner Mongolia, Hebei, and Shanxi. Each productive cow was subsidized with RMB20 ($3.00) for two straws of frozen semen from MOA identified high-quality Holstein bulls. All sizes of operations benefit from this program. The subsidy in 2006 was expanded to cover 178 counties in 22 provinces with a total subsidy of RMB 100 million ($14.93 million). The following year subsidy remained at the same level. In 2008, the subsidy was increased to RMB240 million ($35.82 million) mostly for Holstein cows, and a small number of dairy buffalo cows, Simmental cows, brown cows, and yak cows. In 2009, the subsidy was increased to RMB260 million ($38.8 million) to cover all Holstein cows, and additionally included Jersey cows and Sanhe cows. Each productive Holstein or Jersey cow is now subsidized with RMB30

($4.50) for two straws of frozen semen, while the rest are subsidized with RMB 20 ($3.00) for two straws of frozen semen from MOA identified high-quality dairy bulls.

MOA Launches Demonstration Farms to Promote Standardized Dairy Cow Rearing

In order to teach cow farmers to raise animals more efficiently, MOA started a Program of Building Demonstration Farms for Standardized Livestock and Poultry Rearing in early 2010. MOA requests that selected demonstration farms should have an inventory at least 200 cows and comply with MOA five requests, mainly include 1) high-quality breeds; 2) efficient facilities for animal rearing and environment control; 3) standardized production procedures with computerized management; 4) systemized animal quarantine; 5) good animal waste treatment. The central government will subsidize demonstration farm construction, though amounts allocated for this program are unavailable.

New Dairy Safety Standards, and Full Implementation of Infant Formula Labeling Request

On March 26, the Ministry of Health announced a new national dairy standard**,** altogether 66-items, including 15 product standards, two production standards, and 49 inspection method standards. Raw milk and raw milk related test standards became effective as of June 1, 2010. Pasteurized and UHT milk standards, and dairy GMP standards will be effective on December 1, 2010. Infant formula food standards will become effective on April 1, 2011. For raw milk, the minimum protein content declined from the previous 2.95 to 2.8 percent per 100 grams, while the maximum micro-organism tolerance increased from previous 0.5 million to 2 million per milliliter. In response to the new standards, there have been complaints that since the standards are weaker than those in the west, this will hurt competitiveness of local industry. However, supporters of the standards believe they are realistic in light of the current state of animal husbandry in China, where small scale production and varied feeding environments lead to large differences in the types of dairy cows and quality characteristics within the industry. Small-scale operators in particular will reportedly still have trouble meeting the new 2.8 percent protein standard. While China's dairy processors are opposed to the modifications, domestic dairy farmers welcome the changes, which will make their milk easier to market.

According to the revised "Regulation on Food Labeling Management" announced by AQSIQ on October 22, 2009 in its No. 123 Announcement that that infant formula should indicate main nutrition ingredients and content in product labeling as of the date of announcement. Full implementation started on June 1, 2010.

Consumption

Further Growth in Chinese Milk Consumption in 2011

Post forecasts China's fluid milk consumption in 2011 will rise six percent to 13.1 MMT, following a four percent increase in 2010. Consumption gains are being fueled by continued rapidly rising interest in dairy products, higher disposable incomes, increasing health consciousness among the growing middle class, and expanding retail outlets. Although the dairy market sustained a high rate of growth during the past decade, per capita consumption of dairy products in China, especially in rural areas, is still very low, suggesting the potential for continued strong demand gains for many years to come.

Per Capita Consumption of Dairy Products in 2008 (Kg)

	China	East China	Central China	West China	North-east China
Urban Area [1]	15.19	16.81	12.27	15.46	14.72
Rural Area [2]	*3.43*	*4.37*	*1.87*	*4.01*	*2.73*

Source: 2010 Annual Report from CDIA, National Statistics Bureau

The gap between China's per capita consumption and the average per capita consumption of over 200 kg in developed countries further illustrates the growth potential of China's dairy market. It also explains why China's dairy market, facing so many challenges, has the potential to bounce back quickly after serious set-backs and still show considerable potential for future development.

Post forecasts China's NFDM consumption in 2011 will rise seven percent to 156,000 MT from a considerable 18 percent increase in the previous year fueled by strong demand for infant formula, the primary channel for NFDM shipments. With 17 million babies born every year in China, demand for infant formula will continue to rise, with imported milk powder accounting for nearly all the growth. This channel is also less price sensitive than other products, so demand has been more resilient in the face of the recent rapid run up in prices. Other formula product consumption is also on the rise, such as formulas for aged or high blood sugar patients. Meanwhile, Post forecasts China's WMP consumption in 2010 will rise six percent to 1.5 MMT from an estimated 33 percent increase in the previous year. WMP is normally used for food processing or other dairy product processing, such as bakeries, chocolates, yogurt, and functional formulas for specific consumers like school students, pregnant women, aged, sick people.

Trade

Fluid Milk Imports Up 13 Percent in 2011

While still a small niche market, China's fluid milk imports will continue to rise through 2011. Post forecasts China's fluid milk imports in 2011 will increase 13 percent to 17,000 MT following a 15 percent increase in 2010. The strong demand is fueled by sales to wealthier Chinese and expats who are willing to pay up 20 rmb ($2.94) per liter of imported milk at retail. New Zealand, Australia, and France account for almost 90 percent of sales.

Non-Fat Dry Milk Imports to Continue Higher

Fueled by strong demand from infant formula producers, imports of NFDM are expected to approach 100,000 metric tons in 2011, up from 91,000 metric tons in 2010 and 55,000 tons just two years ago. While traders report food safety concerns are affecting sales in a number of Chinese dairy products, there has been especially weak demand for local milk from manufacturers of infant formula, which accounts for an estimated 10-15 percent of Chinese milk consumption.
Some infant formula processors, such as Shenyuan, have completely shifted to domestic materials due to safety concerns.

Whole Milk Powder Imports in 2011 Strong

Boosted by strong consumer demand and tight domestic supply, Post forecasts China's whole milk powder (WMP) imports in 2011 will increase 24 percent to 420,000 MT, following a 90 percent

increase in 2010. New Zealand and Australia will continue to account for more than 90 percent of total imports.

Post forecasts Chinese dairy product demand will continue to grow faster than local production requiring additional whole milk powder imports through 2011. In response to tight domestic milk supply, and food safety concerns on local milk, many Chinese companies including large-scale manufacturers such as Wahaha, have shifted to imported ingredients for entire production lines. In some cases firms have contracted with foreign companies to manufacture retail products for distribution in the Chinese retail market. China's growing reliance on imports will continue for the foreseeable future.

Whey Imports Dampened by Price Increases

China's 2010 whey imports (through August) are down to 160,000 metric tons, falling 16 percent from the same period in 2009. The slump in imports is reportedly due to sharply higher whey prices and a gradual shift toward more imported lactose mixed with whey protein concentrate, which is considered easier to use than whey. Prices for whey from the United States, the largest supplier, have almost doubled in 2010 compared to the same period last year. Meanwhile price increases for whey protein concentrate are substantially lower. The prospect for sales gains in 2011 will continue to depend largely on whey price vis-à-vis alternative ingredients.

China Lifted Its Ban on Dairy Product Imports from FMD Countries

On September 7, 2010, AQSIQ and MOA jointly announced their No. 99 Decree lifting its ban on dairy product imports from FMD countries. However, imported products must be processed so that they cannot carry FMD viruses and the products must be derived from milk of healthy cows. The ban lifting will not significantly change China's trade pattern because traditional world suppliers to China, such as New Zealand, Australia, the EU and the United States have long dominated China's import market.

New Dairy Certificate Requested

On January 19, 2010, AQSIQ notified to the World Trade Organization (WTO) the Announcement of the Regulation on Sanitary Certificate of Import of Dairy Products, which became effective on March 1, 2010. The new regulation requests exporting countries to certify the status of four animal diseases and that products meet China's food safety requirements for each dairy shipment. Negotiations between FAS/Beijing and AQSIQ regarding the certification of U.S. dairy products are ongoing. Both sides have agreed the existing USDA hygiene certificate for dairy exports to China will be accepted while progress is made toward specific certification language that meets AQSIQ's concerns.

Fluid Milk Exports in 2011 Up, but WMP Exports Poor in 2011

FAS Beijing (Post) forecasts China's fluid milk exports in 2011 will recover 10 percent to 24,000 MT after a 10 percent increase in 2010. Hong Kong accounts for 98 percent of sales. Despite the gains, China's milk exports remain well below levels previous to the melamine crisis (38,400 metric tons in 2008). Meanwhile, Post forecasts China's WMP exports in 2011 will remain flat at 3,000 MT, with Myanmar and New Zealand accounting for nearly all sales. This is down from 62,000 metric tons in 2008.

Marketing

By Susan Zhang, ATO Shanghai

1. Market Size

The Chinese dairy market is still growing strongly. According to Euromonitor statistics, total dairy sales in China reached $ 23,573.8 million in 2009, a nearly 10% increase from 2008. It is estimated that the dairy market is growing another 10% in 2010.

Retail Value of Dairy Markets (million $)

	2005	2006	2007	2008	2009
Dairy Products	15,002.2	17,790.2	20,553.1	21,465.9	23,573.8
Drinking milk products	12,515.4	14713.6	16,857.7	17,408.9	18,898.8
Cheese	60.1	71.1	83.5	99.8	116.4
Yoghurt & sour milk drinks	2,263.4	2,832.2	3,427.2	3,760.5	4,349.7
Other dairy products	163.3	173.3	184.6	196.6	208.9

**Drinking milk products include fluid milk, flavored milk drinks and milk powder etc.*
Source: Euromonitor (Exchange rate between USD and RMB: 1USD to 6.7RMB)

2. Distribution Channels

2.1 Retail channels

In China, nearly 80% of dairy products are consumed through retail channels. Supermarkets and hypermarkets have been evolving into the major outlets for all varieties of dairy products. For cheese products, yogurt and take-home ice cream, the supermarkets' role is even more important due to consumer's confidence in their comparatively better cold chain facilities. Improved availability of supermarkets and convenience stores in rural areas also contributed to their increasing share in the distribution channel.

In 2009, the percentage of all dairy products (whether fluid milk products, cheese, yoghurt or other dairy products) distributed by super and hypermarkets increased further. The proportion distributed by independent small grocers is decreasing. This trend is partly because, after a series of scandals related to dairy products, consumers have relatively more confidence in large scale chained supermarkets/hypermarkets. These not only have more reliable product sourcing channels, but also provide better cold chain facilities to maintain the quality of the dairy products.

Dairy Products Distribution Channel % Breakdown in 2009

Dairy product categories	Supermarkets/ hypermarkets	Independent food stores	Convenience stores	Others
Drinking Milk Products*	32.5	27.5	14.1	25.9
Cheese	93.2	4.9	-	6.8
Yogurt/sour milk drinks	78.2	2.8	14.3	4.7
Other dairy products	78.6	3.0	14.0	4.4

**Drinking milk products include fluid milk and milk powder etc.*
Source: Euromonitor

2.2 Food Service Channels

While competing fiercely in the retail channel, major manufacturers are competing in the food service channel with specially designed brands. Brands such as Angli from Sanyuan, Yiran from Yili, LOOK from Bright Dairy, and Muge from Mengniu are designed to target the food service channel. Although the profit in food service channel may be higher than that achieved from retail channels, manufacturers face high entrance fees, which are determined by hotels and restaurants, and delayed payment. Hotels and restaurants normally pay after they sell the products. This has constrained the sales volume of the dairy products through food service channels.

Yoghurt bars are a restaurant format that is emerging in first tier cities and are becoming popular among younger generation consumers. Competing with juice bars and ice-cream bars, yoghurt bars offer frozen yoghurt and yoghurt drinks of various flavors. These yoghurt bars are generally located in Central Business District (CBD) zones. Their floor space is typically limited, and they have few seats, as most consumers choose take the products to their offices or homes.

2.3 Other channels

Some dairy products, particularly fluid milk, reach consumers through special channels, such as the "school milk program". In this program, milk is delivered to school students directly by government-designated manufacturers who have a good reputation on product quality and safety.

In 1st tier cities including Shanghai and Guangzhou, some consumers still prefer direct delivery of the milk to their home every early morning. Milk directly delivered by manufacturers is perceived as more fresh, and of lower cost.

3. Marketing Tools

Statistics show that dairy product sales growth is directly related to investment in advertising. Hence the major dairy players are investing large amounts in branding and advertising. TV commercials are the most important type of advertising for dairy products targeted at retail channels. The most frequently advertised dairy products in China are fluid milk, infant formula or fortified milk powder with minerals, yogurt, ice cream and dairy drinks. Celebrity endorsement (film stars, singing stars etc.) is frequently used in TV ads.

Some manufacturers have also raised awareness tremendously and strengthened the reputation of their dairy products by sponsoring certain political or entertaining projects with wide public attention. For example, Yili sponsored the 2010 Shanghai World Expo, where only Yili dairy products are available to visitors within the Expo Garden.

China had 600 million internet users by mid 2010. Online marketing is becoming an increasingly efficient platform to promote dairy products through interactive programs. These are typically targeted at younger generation consumers. For example, Coca-cola promoted its flavor milk product Minute Maid via Tencent QQ.

4．Trends of Major Product Categories

4.1 Fluid Milk

There are currently more than 2,000 companies in China involved in fluid milk manufacturing. Fierce competition has forced the profit of fluid milk production to low levels. At the national level, UHT milk had about 73% of the market by volume in 2009, thanks to its availability in markets far from the manufacturing site and comparatively lower retail price. But in big cities where the cold chain infrastructure is better established, pasteurized milk occupies more than 70% of the market.

The competition used to be carried between between UHT milk by resource-oriented manufacturers, represented by Yili and Mengniu from Inner Mongolia, and pasteurized milk by market-oriented manufacturers, represented by Bright Dairy from Shanghai and San Yuan from Beijing. However, in the last two years, traditional pasteurized milk manufacturers (e.g. Bright) began invest in the UHT milk sector heavily, while traditional UHT milk manufacturers (e.g. Mengniu) began to build up farms and pasteurized milk production lines in adjacent to huge consumer markets including Shanghai and Guangzhou. The previously heated debate about whether UHT or pasteurized milk was “more nutritious” or “safer” is no longer seen in the media.

Sales value of fluid milk 2005-2009 ($ Million)

	2005	2006	2007	2008	2009
Fluid milk	6,417.6	7,764.4	8,805.8	8,948.6	9,321.1
Pasteurized milk	1,612.2	1,756.1	1,917.0	1,955.5	2,065.5
UHT/Long life milk	4,805.4	6,008.3	6,888.8	6,993.1	7,255.5

Source: Euromonitor (Exchange rate between USD and RMB: 1vs 6.7)

Burgeoning market demand used to make fluid milk the fastest growing dairy product sector. However, since 2008, two-digit growth has slowed, and the retail value of fluid milk only increased 1.6% in 2008 and 4.2% in 2009. This was far from the growth rates posted by cheese and yoghurt.

At the end of 2009, Mengniu with 22% of the market was the leading fluid milk manufacturer, followed by Yili and Bright Dairy.

Manufacturers have spared no effort to differentiate their products in terms of ingredients, flavors and even packaging. Starting in late 2009, the major manufacturers all launched health fortified products, with various ingredients including grains, beans, jujube, Gouqi berry and even Ejiao, (a gelatin made of donkey-hides and believed good for blood in Chinese medicine) added to the milk.

The children's milk segment, though small in proportion, witnessed strong growth in 2009. The three "Dairy Giants" all launched children's milk products. Among them, Future Star by Mengniu is the leading brand in 2009 and 2010.

More and more foreign fluid milk brands are appearing on the shelves of supermarkets/hypermarkets and import food stores. Successful brands include "Country Goodness" and "Anchor" from New Zealand, "Pauls" from Australia, and "President" from France. Some American milk manufacturers are also evaluating the market opportunities. It is expected that by the end of 2010 some U.S. aseptic milk products with a 6-month shelf life will be launched in 1st tier cities in China.

Following the launch of organic milk products by Yili in 2007 and Mengniu in 2008, more domestic dairy manufacturers launched organic milk brands in 2009 and 2010. These try to address the food safety concerns of high-end consumers. Currently the domestic organic milk brands available in market are Jindian from Yili and Telunsu OMP from Mengniu from Inner Mongolia, Guiyi from Shandong Yinxiang Dairy, Fucheng and Yuantianran from Hebei Province, and Guiyuan from Beijing. Constrained by the strict certification process and high technology requirements as well as the higher price, organic milk production is unlikely to grow rapidly in the near future.

4.2 Cheese

The cheese market is expected to maintain robust growth in 2010. Since 2003, the Chinese cheese market has been growing at an average annual rate of 20%. Although not a part of the traditional Chinese diet, the concept that cheese is a good source of protein and calcium has found its way into the middle class consumers' mind. The prevalence of pizza restaurants and bakery stores also contributed to the fast growth of cheese consumption. According to Euromonitor, sales value of cheese grew by 18% in retail channels, and 13% in food service channels in 2009.

Almost all the cheese available in China market is imported and processed. In 2009 China imported 16,977 metric tons of cheese, 22.1% higher than year before. New Zealand is the biggest cheese exporter to China, taking 51.5% of the import cheese market, followed by Australia (26.4%) and United States (10%). China also imported cheese from France, the Netherlands, Argentina and Italy.

The ratio between spreadable and unspreadable processed cheese was about 35%-65% in 2009. The ratio has been very stable since 2005, with unspreadable processed cheese slightly outperforming spreadable cheese and slowly increasing its shares. Cream cheese dominated the spreadable processed cheese market. For unspreadable cheese, the most frequently available products are Mozzarella, Monterey Jack, Cheddar, and Parmesan cheese.

Leading domestic dairy companies including Bright Dairy, Sanyuan and Yili have all launched cheese processing lines. They have also run very successful consumer education programs. In 2009, Bright Dairy lead cheese sales with 52% of the market, followed by Anchor (18.9%) and Pikifou (6.7%). The top five brands occupy over 85% of the cheese market.

Many foreign brands are available in supermarkets in China. 11 U.S. cheese brands had entered the China market by the end of 2009. Brands including Land O'Lakes and Sargento performed very well. Other major import cheese brands are Kraft from various countries, Mainland from New Zealand, President and Cantorel from France, Bega from Australia, Emmi from Switzerland, Feta from Germany, Arla from Denmark, and Kerry Gold from Ireland.

Currently the key consumers of domestic cheeses are wealthier Chinese consumers, especially health-conscious young parents who believe that cheese improve health of their children. Consumers of foreign brands are mainly foreigners living or traveling in China and returnees from abroad.

In 2009 and 2010, domestic manufacturers launched more innovative flavors including chocolate, tree nuts, strawberry and banana flavors, and cheese products fortified with vitamins and minerals that appeal to Chinese consumers. Many promotions and price discounts were also offered to attract consumers, which lowered the unit price of cheese, and greatly contributed to the sales growth of cheese products.

It is forecast that China's cheese market will continue to grow rapidly in the next five years, and that growth will spread from 1st tier city markets to 2nd and 3rd tier markets. Ongoing economic development will increase Chinese consumers' purchasing power, and make high-priced cheese products more acceptable for mass consumers.

4.3 Yoghurt

The yoghurt market maintained its consistently strong growth in China in 2009. As most yoghurt products are reconstituted (made of milk powder) in China, demand for yoghurt was impacted by reduced consumer confidence after the melamine scandal. Yoghurt retail sales grew by 15.7% in 2009, much higher than the 9.7% growth rate in 2008.

Thanks to long-term consumer education programs, yoghurt is widely perceived a health product that is good for digestion and weight control in China, which appeals to Chinese white collar consumers. Flavor innovation with new ingredients such as jujube, herbs, and cereals contributed greatly to sales growth. Various discount programs increased its attractiveness to even lower income consumers. In

addition to flavor innovation, manufacturers tried to adopt new technology to develop new products that do not need the cold chain, a major constraint for further growth of the product. Following Momchilovtsi, a high-end yoghurt with a shelf life of 90 days launched in January 2009, Bright Dairy launched Hi You Guo Li, another shelf-stable yoghurt with fruits in late 2009. These shelf-stable yoghurt products greatly improved availability in 3rd tier city markets and rural areas.

Bright Dairy, Mengniu, and Yili were the domestic leaders in this sector in 2009. Danone, which used to be the No. 1 yoghurt brand in China before 2007, faced the embarrassing situation of lacking a manufacturing site and sales team after failing to form a partnership with Mengniu and Bright consecutively. However, in 2009, Danone yoghurt returned to market after acquiring the Beijing Miaoshi yoghurt plant, and is gaining a stronger presence in market in 2010.

Imported yoghurt enjoys a stable but small growth rate, as its loyal consumers are mainly expatriates or returned overseas Chinese. Emmi from Switzerland, Elle & Vive from France, Yoplait from Australia and FAGE from Greece are frequently available brands on the shelves of import food supermarkets/stores.

Meanwhile, some smaller manufacturers explored niche markets, striving to achieve unique values created through innovation in products, branding and marketing. Frozen yoghurt is one of them. In 2009, the frozen yoghurt brand "Qin Hai Old Yoghurt" by Xiao Xi Niu from Qinghai Province gained a great success, with its sales tripled from RMB 40 million in 2008 to RMB 130 million in 2009. Yoghurt bars – small footprint restaurants that serve yoghurt-based flavored desserts - have emerged as strong competitors to juice bars and ice cream bars.

4.4 Milk Powder

Milk powder production reached a peak in 2007, and has been decreasing since 2008 in both production and retail value. In 2009, milk powder sales dropped by 18% from 2008 to $ 1,749.4 million.

In 2009, China found it difficult to export milk powder to overseas markets. Meanwhile, due to low dairy prices in international market, a large quantity of low-priced milk powder was imported into China. Entry ports were mainly in north China, east China, and central-south China. Imports were increasing so fast that MOFCOM sent out warning in early 2010 to remind importers about the risks of oversupply of milk powders in the market.

In contrast, infant formula milk powder sales grew steadily. In 2009, total sales of infant formula milk powder amounted to $ 4,421.9 million, registering an increase of 16.2% over 2008 according to Euromonitor statistics. The high value-added infant formula milk powder market is nearly monopolized by multinational giants from Europe, United States, and Australia. Apart from the advantages in technology, foreign companies also enjoy a competitive edge in branding and channel management. In addition, foreign brand infant formula also enjoys higher trust among Chinese consumers. Foreign infant formula brands raised prices several times during the past one year, but concerns about food safety have made young parents in China less price sensitive.

The top 5 international brands - International Nutrition (Dumex), Mead Johnson (Enfagrow, Enfapro, Enfachild, Enfaschool), Abbott Nutrition International (Gain, Similac), Nestle (Lactogen, Neslac), and Wyeth (Promise, S-26, Bright Promil) - took over 50% of the market. Beingmate overtook Yili from Inner Mongolia, Shengyuan from Qingdao, Yashili from Guangdong, and Wonder Sun from Heilongjiang to become the star performer among domestic brands. Not implicated in the melamine

scandal in 2008, the Hangzhou-headquartered Beingmate saw a significant increase in its sales and consumer awareness. With over 200 baby food products in its portfolio, Beingmate's sales revenue exceeded RMB 10 billion ($ 1.5 billion) in 2009. In June 2010, Beingmate submitted IPO application and is expected to become publicly listed by end of 2010.

Dairy Statistics

Fluid Milk PS&D Table

Dairy, Milk, Fluid China	2009 Market Year Begin: Jan 2009 USDA Official	Old Post	New Post	2010 Market Year Begin: Jan 2010 USDA Official	Old Post	New Post	2011 Market Year Begin: Jan 2011 USDA Official	Old Post	New Post	
Cows In Milk	7,115	0	7,115	7,632		7,350			7,630	(1000 HEAD)
Cows Milk Production	28,445	0	28,445	31,290		29,100			30,500	(1000 MT)
Other Milk Production	1,180	0	1,180	1,225		1,228			1,280	(1000 MT)
Total Production	29,625	0	29,625	32,515		30,328			31,780	(1000 MT)
Other Imports	12	0	13	15		15			17	(1000 MT)
Total Imports	12	0	13	15		15			17	(1000 MT)
Total Supply	29,637	0	29,638	32,530		30,343			31,797	(1000 MT)
Other Exports	19	0	20	13		22			24	(1000 MT)
Total Exports	19	0	20	13		22			23	(1000 MT)
Fluid Use Dom. Consum.	11,791	0	11,791	13,225		12,010			12,500	(1000 MT)
Factory Use Consum.	17,817	0	17,817	19,292		18,311			19,274	(1000 MT)
Feed Use Dom. Consum.	10	0	10	0		0			0	(1000 MT)
Total Dom. Consumption	29,618	0	29,618	32,517		30,321			31,774	(1000 MT)
Total Distribution	29,637	0	29,638	32,530		30,343			31,797	(1000 MT)
CY Imp. from U.S.	0	0	0	0		0			0	(1000 MT)
CY. Exp. to U.S.	0	0	0	0		0			0	(1000 MT)
TS=TD			0			0			0	

Non-Fat Dry Milk PS&D Table

Dairy, Milk, Nonfat Dry China	2009			2010			2011			
	Market Year Begin: Oct 2009			Market Year Begin: Oct 2010			Market Year Begin: Oct 2011			
	USDA Official	Old Post	New Post	USDA Official	Old Post	New Post	USDA Official	Old Post	New Post	
Beginning Stocks	0		0	0		0			0	(1000 MT)
Production	54		54	55		55			56	(1000 MT)
Other Imports	65		70	70		91			100	(1000 MT)
Total Imports	65		70	70		91			100	(1000 MT)
Total Supply	119		124	125		146			156	(1000 MT)
Other Exports	0		0	0		0			0	(1000 MT)
Total Exports	0		0	0		0			0	(1000 MT)
Human Dom. Consumption	119		124	125		146			156	(1000 MT)
Other Use, Losses	0		0	0		0			0	(1000 MT)
Total Dom. Consumption	119		124	125		146			156	(1000 MT)
Total Use	119		124	125		146			156	(1000 MT)
Ending Stocks	0		0	0		0			0	(1000 MT)
Total Distribution	119		124	125		146			156	(1000 MT)
CY Imp. from U.S.	6		6	5		12			15	(1000 MT)
CY. Exp. to U.S.	0			0						(1000 MT)
TS=TD			0			0			0	

Whole Milk Powder PS&D Table

Dairy, Dry Whole Milk Powder China	2009			2010			2011			
	Market Year Begin: Jan 2009			Market Year Begin: Jan 2010			Market Year Begin: Jan 2011			
	USDA Official	Old Post	New Post	USDA Official	Old Post	New Post	USDA Official	Old Post	New Post	
Beginning Stocks	120		120	110		110			60	(1000 MT)
Production	977		977	1,030		1,000			1,050	(1000 MT)
Other Imports	165		177	150		340			420	(1000 MT)
Total Imports	165		177	150		340			420	(1000 MT)
Total Supply	1,262		1,274	1,290		1,450			1,530	(1000 MT)
Other Exports	12		10	10		3			3	(1000 MT)
Total Exports	12		10	10		3			3	(1000 MT)
Human Dom. Consumption	1,050		1,064	1,210		1,357			1,507	(1000 MT)
Other Use, Losses	90		90	10		10			5	(1000 MT)
Total Dom. Consumption	1,140		1,154	1,220		1,387			1,477	(1000 MT)
Total Use	1,152		1,164	1,230		1,390			1,480	(1000 MT)
Ending Stocks	110		110	60		60			50	(1000 MT)
Total Distribution	1,262		1,274	1,290		1,450			1,530	(1000 MT)
CY Imp. from U.S.	1		0	1		0			0	(1000 MT)
CY. Exp. to U.S.	0		0	0		0			0	(1000 MT)
TS=TD			0			0			0	

Dairy Trade Matrices

China Fluid Milk Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	7,565	12,763	7,710	9,626	24.85
New Zealand	3,567	5,577	3,515	4,235	20.48
France	1,320	2,128	1,311	2,460	87.64
Germany	429	1,678	832	1,627	95.55
Australia	1,719	1,601	989	889	-10.11
South Korea	178	1,196	657	37	-94.37
United States	12	36	33	16	-51.52
Other	340	547	373	362	-2.95
HS Codes: 0401.1000, 0401.2000, and 0401.3000 Source: GTA China Customs Statistics					

China Non-Fat Milk Powder Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	54,965	70,443	45,761	60,009	31.14
New Zealand	18,122	46,515	31,380	35,911	14.44
United States	15,601	6,012	3,072	7,909	157.45
Australia	14,455	10,179	7,150	4,362	-38.99
Germany	1	1,944	1,301	2,285	75.63
France	1,249	766	349	2,009	475.64
Ireland	758	424	272	1,287	373.16
Netherlands	122	1,152	1,052	990	-5.89
Belgium	475	539	1	668	66700.00
Canada	1,278	1,050	300	650	116.67
Finland	2	402	352	607	72.44
Switzerland	0	525	425	578	36.00
Argentina	0	0	0	504	0.00
Belarus	0	525	0	500	0.00
India	2,652	0	0	0	0.00
Other	250	410	107	1,749	1534.58
HS Codes: 0402.1000 Source: GTA China Customs Statistics					

China Whole-Fat Milk Powder Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	45,965	177,345	117,355	226,650	93.13
New Zealand	32,471	157,395	101,122	201,750	99.51
Australia	9,974	7,873	5,664	12,212	115.61
Denmark	4	2,425	1,617	3,356	107.54
Belgium	137	29	8	2,375	29587.50
Chile	25	0	0	1,550	0.00
Uruguay	0	0	0	1,125	0.00
France	2,102	6,209	5,819	778	-86.63
Singapore	23	9	7	703	9942.86
United Kingdom	0	25	0	640	0.00
Argentina	16	3	3	600	19900.00
Netherlands	78	2,251	2,201	584	-73.47
United States	885	51	14	283	1921.43
Germany	68	142	125	200	60.00
Poland	50	600	500	0	-100.00
Other	132	333	275	494	79.64
HS Codes: 0402.2100, 0402.2900, 0402.9100, and 0402.9900 Source: GTA China Customs Statistics					

China Whey Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	211,796	287,537	192,217	160,494	-16.50
United States	90,478	140,012	95,488	88,035	-7.81
France	50,672	49,758	31,816	20,464	-35.68
Germany	9,747	15,107	10,522	9,487	-9.84
Finland	9,936	14,148	9,473	8,784	-7.27
Netherlands	12,184	13,745	9,287	6,757	-27.24
Australia	8,609	8,930	6,300	4,770	-24.29
Ireland	8,630	13,070	8,637	3,886	-55.01
New Zealand	6,734	3,701	3,160	3,886	22.97
Poland	1,807	5,778	4,161	3,433	-17.50
Ukraine	1,875	3,175	1,950	2,875	47.44
Argentina	2,817	5,767	3,435	2,447	-28.76
Canada	3,880	7,610	4,879	1,709	-64.97
Austria	308	2,166	800	1,195	49.38
Uruguay	0	250	150	1,195	696.67
India	2,258	384	336	560	66.67
Spain	96	1,396	864	360	-58.33
Italy	443	646	222	126	-43.24
Belgium	435	528	432	120	-72.22
Other	887	1,366	305	405	32.79
HS Codes: 0404.1000 and 0404.9000 Source: GTA China Customs Statistics					

China Butter and Dairy Spread Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	7,904	17,569	10,801	10,294	-4.69
New Zealand	5,704	14,045	8,506	7,788	-8.44
Australia	923	1,952	1,365	1,164	-14.73
France	517	509	364	510	40.11
Argentina	90	77	77	298	287.01
United States	164	112	80	140	75.00
Belgium	73	54	9	99	1000.00
Netherlands	202	229	166	79	-52.41
Finland	82	274	124	0	-100.00
Other	149	317	110	216	96.36
HS Codes: 0405.1000, 0405.2000, and 0405.9000 Source: GTA China Customs Statistics					

China Cheese Imports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	13,904	16,978	9,473	15,139	59.81
New Zealand	6,233	8,735	4,610	7,468	62.00
Australia	3,432	4,490	2,588	3,710	43.35
United States	1,998	1,691	1,049	1,911	82.17
France	445	326	219	339	54.79
Italy	216	242	164	215	31.10
Denmark	166	139	90	173	92.22
Uruguay	175	50	50	165	230.00
Netherlands	119	345	237	161	-32.07
Germany	401	168	70	149	112.86
Other	719	792	396	848	114.14
HS Codes: 0406.1000, 0406.2000, 0406.3000, 0406.4000, and 0406.9000 Source: GTA China Customs Statistics					

China Fluid Milk Exports, 2008-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	38,428	20,030	12,724	14,467	13.70
Hong Kong	28,114	19,864	12,614	14,325	13.56
Macau	1,860	165	110	118	7.27
Philippines	2,496	0	0	0	0.00
Singapore	1,983	0	0	0	0.00
Mongolia	1,897	0	0	0	0.00
Libya	1,290	0	0	0	0.00
Other	788	1	0	24	0.00
HS Codes: 0401.1000, 0401.2000, and 0401.3000 Source: GTA China Customs Statistics					

China Whole-Fat Milk Powder Exports, 2009-2010 (Year-To-Date) (Metric Tons)					
	Jan-Dec	Jan-Dec	Jan-Aug		Jan-Aug
	Quantity	Quantity	Quantity Comparison		% Change
Origin	2008	2009	2009	2010	2010/2009
World	62,387	9,737	8,251	2,110	-74.43
Myanmar	2,773	1,519	1,100	1,052	-4.36
Singapore	280	2	0	731	0.00
Hong Kong	2,006	54	35	206	488.57
Thailand	3,126	77	58	39	-32.76
Taiwan	7,732	25	12	37	208.33
Mongolia	682	0	0	12	0.00
Venezuela	35,530	5,250	5,250	0	-100.00
Nigeria	3,027	2,567	1,683	0	-100.00
United Arab Emirates	799	46	46	0	-100.00
Sudan	944	0	0	0	0.00
Saudi Arabia	609	0	0	0	0.00
Mauritania	515	0	0	0	0.00
Vietnam	332	57	42	0	-100.00
Lebanon	389	0	0	0	0.00
Bangladesh	220	0	0	0	0.00
Iraq	677	128	0	0	0.00
Turkey	185	0	0	0	0.00
Other	2,561	12	25	33	32.00
HS Codes: 0402.2100, 0402.2900, 0402.9100, and 0402.9900 Source: GTA China Customs Statistics					

China Average Milk Prices, 2008-2010 (Year-to-Date) (RMB/KG, $1=RMB6.69)				
MONTH	2008	2009	2010	% Change 2010/09
January	2.98	2.79	3.02	8.24
February	3.03	2.74	3.04	10.95
March	2.96	2.69	3.10	15.24
April	2.94	2.65	3.16	19.25
May	2.93	2.61	3.23	23.75
June	2.98	2.59	3.31	27.80
July	2.86	2.60	3.27	25.77
August	2.81	2.60		
September	2.81	2.61		
October	2.79	2.65		
November	2.80	2.68		
December	2.82	2.75		
Source: The Ministry of Agriculture				

End report